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C O N F I D E N T I A L SECTION 01 OF 03 ANKARA 008594

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E.O. 12958: DECL: 11/20/2012
TAGS: EINV ENRG ECON PREL TU
SUBJECT: UNCERTAINTY FOR PENDING AND EXISTING BOT/TOR
PROJECTS IN TURKEY

REF: A) ANKARA 4740 B) ANKARA 3892

Classified by DCM Robert Deutsch; reasons: 1.5 (b,d).

¶11. (C) Summary and comment: Embassy has long emphasized to the GOT the importance of a rapid and fair settlement to the pending BOT/TOR projects, which still have not been resolved (reflets). It now appears the GOT is considering re-negotiation of the contracts for the BOT projects that are already in operation, including U.S.-owned companies Trakya Elektrik (Enron) and Doga Enerji (Edison Mission). Trakya and Doga have filed suit against the government, claiming that recently announced regulations are in violation of their contracts, and are intended to force the companies to lower their prices. As we engage the new government on economic matters, we will couple our support for their overall energy liberalization efforts with an emphasis on the importance of contract sanctity.

Existing BOT Projects Fear Contracts Will Be Reopened

¶12. (C) A year after being established, the Energy Market Regulatory Authority (EMRA) is still grappling with how to handle the pending build-operate-transfer (BOT) and transfer-of-operating rights (TOR) energy projects. Unfortunately, EMRA is also now reevaluating the six BOT projects that are already in operation, which include the U.S.-owned, OPIC-financed energy companies Trakya Elektrik (Enron) and Doga Enerji (Edison Mission). (Note: Enron's share in Trakya Elektrik is reportedly being sold by the bankruptcy court in the U.S. on November 22).

¶13. (C) Trakya Elektrik and Doga Enerji filed suit against EMRA on October 3, claiming that the electricity market regulations released by EMRA in August constitute a breach of their implementation contracts. The companies have requested an injunction on implementation of those articles of the regulations that could ultimately affect their contracts. For example, the new regulations require all companies -- even those already in operation -- to apply for operating licenses. The new regulation also stipulates that companies must adhere to all existing and future changes to the regulations, which Trakya and Doga claim opens their contracts to unilateral modifications.

¶14. (C) Although EMRA President Yusuf Gunay told us the requirement for existing operators to apply for a license is a "formality," the BOT companies see it as a means for EMRA to reopen negotiations on the prices in the contracts. Various GOT officials have long claimed that the BOT prices for electricity are too high. (Note: the BOTs are charging in the range of 10-12 cents per kilowatt hour. In comparison, the new Intergen BO plants charge in the range of 4-6 cents per kilowatt hour. End note.) The BOT companies argue that their prices accurately reflect the level of risk and higher costs they faced when they signed the contracts in 1993, and when they built the plants in the late 1990s. However, the companies assert (correctly, in our view), whether or not the GOT believes the prices are too high, the fact remains that these are the prices stipulated in the contracts signed by the GOT after years of negotiation.

¶15. (C) Conversations with EMRA's legal advisor and others indicate that Trakya and Doga's suspicions that EMRA will reopen their contracts are not unfounded. Ali Ulusoy, a university law professor, heads an independent commission

enlisted by EMRA to provide recommendations on how to manage the roughly 100 pending and existing BOT, BO, and TOR projects as Turkey liberalizes its energy market. Ulusoy emphasized to econoff that he believes the existing BOTs must reduce their prices, claiming that "otherwise we will not be able to move to a liberalized market." Ulusoy stated that the BOT companies should be "willing to renegotiate" prices in the interest of supporting a free energy market in Turkey, which in the long-term should provide companies with more opportunities. Responding to econoff's point that Turkey would likely pay in terms of decreased FDI if potential investors concluded that the GOT did not honor its contracts, Ulusoy responded that Turkey had "no other option" if it wanted to achieve a free energy market in the next several years.

16. (C) The General Manager of Uni-Mar, one of the non-U.S. BOT companies, told econoff it was clear that EMRA's intention was to force the BOTs to cut their prices. He said that even if there was room for some "flexibility" on the price issue, contractually the companies were under no obligation to renegotiate with the GOT. For this reason, Uni-Mar joined Trakya Elektrik and Doga in their October 3 lawsuits. TETTAS General Manager Hayrettin Yildirim also told econoff the GOT wanted the BOTs to cut their prices.

Meanwhile, No Progress on Pending BOT/TOR Projects

17. (C) As reported Ref A, there has been no progress toward resolution of the pending BOT/TOR projects since former Ministers Cakan and Dervis committed in May to settle all pending signed contracts as soon as possible. As of September 3, when the electricity market law went into force, EMRA took over responsibility for settling these projects. EMRA President Yusuf Gunay recently told emboffs he is still working on a strategy for managing the pending BOT/TOR contracts, noting that he believes EMRA should act as a "mediator" between the signators of the contracts, i.e. the companies and the Ministry of Energy. However, Gunay, as well as legal advisor Ulusoy, made clear that the companies must be flexible on the issues of price and treasury guarantees.

Role of the New Government

18. (C) The AK party announced in its "emergency action plan" on November 16 that it would complete the pending TOR projects within one year. According to several GOT and energy company officials, this policy is being driven by Afif Demirkiran, newly-elected AK parliamentarian and former General Manager of three of the pending TOR projects. Some company representatives believe the election of Demirkiran bodes well for the BOT projects as well, since it would be difficult for the government to treat the BOT and TOR projects differently. AK's emergency action plan also calls for opening the energy market to competition and cutting electricity prices.

19. (C) Turkish Electricity Trade and Contracting Company (TETTAS) General Manager Hayrettin Yildirim told econoff November 20 that Minister of Energy Guler had asked senior MENR officials for their recommendations on energy-related issues. Yildirim, who previously headed Treasury's foreign investment office, had recommended the new government immediately announce its intention to honor all existing contracts, arguing that to do otherwise would do untold damage to Turkey's foreign investment climate. Yildirim said his argument should resonate with the new minister, since it was actually in the interest of TETTAS -- which purchases electricity from the BOTs -- for the government to renegotiate the prices of the existing BOT projects and not to implement the pending BOT/TOR contracts. Yildirim said the electricity from the six operational BOTs comprised about 11 percent of all of TETTAS' electricity purchases. Although the prices may be high by 2-3 cents per kilowatt hour, he estimated the total extra cost to the government (if it honored the contracts) would only be about USD 200 million. Yildirim said that was a small price to pay to avoid companies going to international arbitration and discouraging potential investors.

Comment

110. (C) We have long emphasized to the GOT the importance of honoring its contracts; however, our focus has been primarily on the pending BOT/TOR projects (reflets). It appears that some officials are now considering re-opening the contracts

of the BOT projects that are already in operation. We agree with AK that electricity is relatively expensive in Turkey; however, high prices are not only a result of the BOT plants -- the high price BOTAS pays and charges for gas, inefficient distribution networks, and low bill collection rates also play an important role. Although it is not yet clear how AK intends to handle the pending or existing energy projects, we will emphasize to the new government that, while the U.S. supports establishment of a free energy market in Turkey, the GOT cannot expect to attract more foreign investment unless it honors its existing contracts, or adequately compensates investors when it cannot do so. End comment.

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